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No. 93-332

In the Supreme Court of the United States

OCTOBER TERM, 1993

MICHIGAN MUNICIPAL COOPERATIVE GROUP, ET AL.,
PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

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QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission properly found that a public utility did not own more than 50% of a cogeneration facility and that therefore the facility was entitled to be certified as a "qualifying cogeneration facility" under the applicable statutory provisions and regulations.

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OPINIONS BELOW

The judgment order of the court of appeals (Pet. App. 1a-2a) is unpublished, but it is noted at 990 F.2d 1377 (Table). The opinions of the Federal Energy Regulatory Commission (Pet. App. 5a-113a, 114a-153a, 154a-185a, 186a-207a) are reported at 50 F.E.R.C. ¶ 61,098; 50 F.E.R.C. ¶ 61,259; 56 F.E.R.C. ¶ 61,177; and 56 F.E.R.C. ¶ 61,361.

JURISDICTION

The judgment of the court of appeals (Pet. App. 1a-2a) was entered on March 26, 1993. A petition for

rehearing was denied on June 2, 1993. Pet. App. 3a. The petition for a writ of certiorari was filed on August 31, 1993. Petitioners invoke the jurisdiction of this Court under 28 U.S.C. 1254(1).

STATEMENT

1. Section 210(a) of the Public Utility Regulatory Policies Act of 1978 (PURPA), 16 U.S.C. 824a-3(a), directs the Federal Energy Regulatory Commission (FERC) to prescribe rules under which electric utilities must provide power to and purchase surplus power from "qualifying cogeneration facilities." Section 201(18)(A) of PURPA, 16 U.S.C. 796(18)(A), defines a "cogeneration facility" as "a facility which produces—(i) electric energy, and (ii) steam or forms of useful energy (such as heat) which are used for industrial, commercial, heating, or cooling purposes." The statute defines a "qualifying cogeneration facility" (QF) as a cogeneration facility that, *inter alia*, "is owned by a person not primarily engaged in the generation or sale of electric power (other than electric power solely from cogeneration facilities or small power production facilities)." 16 U.S.C. 796(18)(B).

To implement the congressional restriction limiting ownership of a QF to "a person not primarily engaged in the generation or sale of electric power," the Commission promulgated a rule in 1980 providing that not "more than 50 percent of the equity interest in the facility * * * [may be] held by an electric utility or utilities, or by an electric utility holding company, or companies, or any combination thereof." 18 C.F.R. 292.206(b). In applying that rule in the case of a cogeneration facility owned by a partnership, in which equity interests cannot be measured by common stock holdings, the Commission analyzes the utility's

equity interest by analyzing the utility's share of the facility's "stream of benefits," based on the utility's entitlement to profits, share of losses, and allocation of surplus after the return of its initial capital contribution, as well as the utility partner's share of "control" over the venture. See, *e.g.*, *Ultrapower 3*, 27 F.E.R.C. ¶ 61,094, at 61,184 (1984); *KP Diversified Investors, Inc.*, 32 F.E.R.C. ¶ 61,013 (1985); *Dominion Resources*, 43 F.E.R.C. ¶ 61,079 (1988).

2. This case arises from the plan of Consumers Power Company (CPC), a gas and electric utility serving customers in Michigan, to convert its abandoned nuclear plant in Midland, Michigan, into a gas-fired cogeneration plant. In 1987 CMS Midland, a subsidiary of CPC, entered into an agreement with other companies to form a partnership, the Michigan Cogeneration Venture Partnership (MCV), that would purchase certain assets of CPC's abandoned nuclear plant for approximately $1.5 billion, use the assets to construct a cogeneration facility (the Midland facility), and then sell the electric energy it produced to CPC. CMS Midland filed an unopposed application with the Commission to certify the project as a QF, and the Commission granted QF certification based on CMS Midland's representation that any equity interest held by a public utility would not exceed 50% by the time the facility went into operation. *CMS Midland, Inc.*, 38 F.E.R.C. ¶ 61,244 (1987).

Subsequently, the structure of MCV was significantly altered. See Pet. App. 10a-16a. The partnership now consisted of six partners not affiliated with CPC or an electric utility, and CMS Midland, the CPC subsidiary. Under the new arrangement, CMS Midland's voting interest in the facility was

limited to 49%, and its allocation of profits, losses, and tax and other benefits was reduced to 49%. CMS Midland was also barred from participating in negotiations to determine the consideration to be paid by the partnership to another CPC subsidiary for the abandoned Midland nuclear plant assets. In August 1989, the non-CMS partners agreed to pay the CPC subsidiary approximately $1.2 billion for the Midland assets, subject to a downward or upward adjustment (to a maximum of $1.5 billion) based on the ultimate "avoided cost" finding that, under PURPA, determines the price that the QF could charge for its power. See 16 U.S.C. 824a-3(d).

After the facility had gone into operation, MCV submitted two applications to FERC for recertification of the Midland facility as a QF. The first application reflected the addition of the new partners and certain changes in the technical configuration of the plant, and the second requested the Commission to certify that a proposed sale and leaseback of the facility (see Pet. App. 118a-122a) would not interfere with the facility's QF status.[1]

Petitioners intervened in both proceedings. They urged the Commission to deny the applications on the ground that the proposed arrangements failed to satisfy the Commission's "stream of benefits" and "control" tests because, when the amount of the partnership's payments for CPC's Midland plant assets was taken into account, CPC would actually "control" MCV, within the meaning of FERC's ownership test.

[1] Sales and leasebacks are a common means of financing cogeneration projects and were specifically contemplated by Congress in enacting PURPA. See *Puerto Rico Elec. Power Auth.* v. *FERC*, 848 F.2d 243, 248 (D.C. Cir. 1988).

3. In an order issued January 31, 1990 (Pet. App. 5a-113a), the Commission concluded that the Midland facility qualified as a QF. *Id.* at 36a-37a.

The Commission found that the partnership agreement limited CMS Midland's voting rights and its rights to profits, losses, and surplus to 49% and that no other provision in the agreement would alter the fact that CMS Midland's right to the stream of benefits from the project would not exceed that limitation. Pet. App. 40a-44a.

The Commission also rejected petitioners' claim that CMS Midland retained more than 49% control over the operations of the facility because important decisions regarding the facility's basic operations had already been made by CPC before it had restructured the ownership of MCV. Pet. App. 72a. Agreeing with CMS Midland that FERC's regulation governing certification, 18 C.F.R. 292.206, is applied as of the date the "facility enters initial operation—not before" (Pet. App. 71a-72a), the Commission concluded that CPC could not be deemed to have denied the other partners effective control "by virtue of having structured all the salient agreements pertaining to MCV operation prior to effecting the transfer" of the facility. *Id.* at 72a. Moreover, the Commission concluded from its experience with cogeneration financing that it "is not atypical" for a cogeneration developer to have such matters as fuel supply and power purchase contracts in place before seeking equity investors as partners. *Ibid.* The Commission further observed that "the non-CMS general Partners do have control, not merely by virtue of the fact that they have 51% of the management committee voting power, but also by virtue of the fact that that power

means they may act to affect MCV business dealings" in the future. *Ibid.*

The Commission also determined that CPC's transactions with MCV did not afford CPC any special advantages, such as service contracts with favorable terms or the right to loan money to the partnership at noncommercial interest rates, that might reflect a disproportionate share of the expected stream of benefits from the project. Pet. App. 73a-77a. The Commission likewise concluded that the contracts between MCV and CPC for the sale of power generated by the facility to CPC contained no "hidden benefit" for CPC. *Id.* at 76a. Accordingly, the Commission ruled that there was no obstacle to certifying the facility as a QF.

On March 1, 1990, the Commission issued a second recertification order determining that the sale and leaseback of the facility were consistent with the facility's QF status. Pet. App. 114a-153a.

4. Petitioners sought rehearing of both Commission orders, but the Commission denied rehearing. Pet. App. 154a-185a, 186a-207a.

5. On March 26, 1993, the court of appeals affirmed the Commission's orders without opinion, "substantially for the reasons stated [in the FERC orders]." Pet. App. 2a.

ARGUMENT

The decision of the court of appeals upholding the Commission's fact-based finding that no more than 50% of the MCV facility is owned by a public utility is correct and is not in conflict with any decision of any other court. The Commission's finding is, moreover, based on substantial evidence and the Commission's

settled interpretation of its own regulations. Further review by this Court therefore is not warranted.

1. Petitioners chiefly argue (Pet. 15-23) that the Commission overlooked evidence showing that, although CPC formally owns only a 49% interest in MCV, the balance is tipped to majority control when other factors are taken into account. Relying on the Commission's "stream of benefits" test, petitioners argue that CPC realized additional benefits by obtaining an inflated price from MCV for its plant assets (Pet. 16-20), by entering into advantageous long-term contracts with MCV (Pet. 20-21), and by obtaining a variety of other benefits (Pet. 21-22).

The Commission properly found that petitioners' claims in this regard are unavailing. For example, as the Commission explained, the plant assets were valued by the non-affiliated members of MCV in negotiations from which any CPC affiliate was excluded from participating on MCV's behalf. The methodology for valuing the assets was reasonable and did not reflect exercise of any market power by CPC,[2] and the

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[2] Specifically, the Commission found that it was reasonable to value the assets in terms of the expected revenue stream that they could produce. See Pet. App. 55a-56a. Although that is not the only possible way to value an asset, it certainly is a permissible way to do so. That method was perhaps particularly appropriate in this case, because the revenue stream itself is fixed by the Michigan Public Service Commission's determination of CPC's "avoided cost"—*i.e.*, the amount that CPC would have had to pay for the same power from a non-QF source. See p. 11, *infra*. In other words, if the assets sold to MCV could profitably produce power for which MCV could charge a competitive rate, it was reasonable for FERC to conclude that those assets have a value that is commensurate with what MCV paid for them.

unaffiliated partners conducting the negotiations were able to extract significant concessions from the CPC-affiliated owner. Pet. App. 54a-56a. Similarly, the Commission found that MCV's long-term contracts with CPC reflected prestructuring of business arrangements typical of cogeneration financing; that the contracts were negotiated prior to initiation of the plant's operation, by which time the CPC affiliate's interest was below the 50% limitation; and that the unaffiliated partners controlled the MCV management committee, which was responsible for overseeing the contracts. *Id.* at 72a.

Based on those findings, the Commission was justified in concluding that, as of the time the MCV facility went into operation, CPC did not "control" the facility, and that CPC's ownership interest in the facility therefore posed no obstacle to certification of the facility as a QF under the Commission's regulations.

2. Petitioners also argue (Pet. 23-25) that FERC failed to give preclusive effect to the findings of the Michigan Public Service Commission regarding the close relationship between CPC and MCV, contrary to this Court's decisions in *University of Tennessee* v. *Elliott*, 478 U.S. 788 (1986), and *United States* v. *Utah Construction & Mining Co.*, 384 U.S. 394 (1966).

Initially, petitioners' argument that FERC inappropriately rejected findings of the Michigan Public Service Commission was advanced only in a supplemental filing that FERC rejected as untimely. See Pet. App. 159a, 168a. Although FERC also rejected petitioners' argument on its merits in an alternative holding, see *id.* at 174a-176a, petitioners' failure properly to present their argument to FERC provides

an independent basis for FERC's rejection of their argument and for the court of appeals' affirmance on this point.

In any event, petitioners' reliance on *Elliott* and *Utah* is misplaced. Issue preclusion arises only when another forum has decided the same issue or fact in earlier litigation between the same parties or their privies. See, *e.g.*, *Parklane Hosiery Co.* v. *Shore*, 439 U.S. 322, 326 (1979). As the Commission pointed out, the Michigan Public Service Commission did not find that CPC had power to direct the MCV project, and thereby divert the stream of benefits, or that CPC "controlled" MCV within the meaning of FERC's PURPA regulations. Pet. App. 172a-175a. Findings of the Michigan Public Service Commission on other issues could not preclude FERC's authority to determine the application of its regulations to this case.

In addition, neither *University of Tennessee* v. *Elliott*, *supra*, nor *United States* v. *Utah Construction & Mining*, *supra*, involved the preclusive effect of a prior determination on a later federal administrative proceeding. And in *Elliott*, the Court held that findings of a state administrative agency should *not* be given preclusive effect in federal court Title VII litigation, see 478 U.S. at 795-796, though they may have such effect in civil rights litigation under other federal statutes. See *id.* at 796-799. In each instance, the scope of preclusion depended on the particular statutory scheme at issue. See also *Astoria Federal Sav. & Loan Ass'n* v. *Solimino*, 111 S. Ct. 2166, 2169 (1991). This case arises under PURPA, which explicitly divides authority between FERC and state public utility agencies and which gives FERC—not the state agency—authority to

determine whether a cogeneration facility is entitled to QF status. See 16 U.S.C. 796(18)(B).

Finally, the court of appeals reviewed the decision in this case under a statute providing that "[t]he finding of the Commisssion as to the facts, if supported by substantial evidence, shall be conclusive." 16 U.S.C. 825*l*(b). That standard of review demonstrates Congress's intent to give FERC substantial discretion to reach its own determinations based on the record before it. In light of that standard, even if a FERC order disagreed with a prior state administrative finding, and even if the disagreement revolved around a particular question of historical fact, the court of appeals would have no choice but to affirm the FERC order so long as it was supported by substantial evidence in the record before FERC.

3. Petitioners argue (Pet. 25-30) that FERC's orders will encourage utilities to invest in cogeneration facilities and thereby undermine the competitive goals of PURPA and the consumer protection goals of the Federal Power Act, of which PURPA is a part.

Petitioners' argument is insubstantial. Congress sought to foster cogeneration through various rate and deregulatory incentives contained in PURPA. See *American Paper Institute, Inc.* v. *American Electric Power Service Corp.*, 461 U.S. 402, 406-407, 413-418 (1983). As the Commission pointed out when it adopted its cogeneration regulations, Congress intended that utilities could participate in cogeneration projects. Order No. 70, 1977-1981 Stats. & Regs. [Regs. Preamble] (CCH) ¶ 30,134, at 30,953 & n.29 (1980), citing the Conference Report on H.R. 4018, 95th Cong., 2d Sess. (1978) (PURPA), H.R. Conf. Rep.

No. 1750, 95th Cong., 2d Sess. 89 (1978). FERC's regulations properly implemented those congressional goals. To the extent that petitioners disagree with that conclusion, their complaints are tantamount to an impermissible collateral attack on FERC's regulations, which were adopted in 1980 and upheld by this Court in *American Paper Institute*. See, *e.g.*, *Raton Gas Transmission Co.* v. *FERC*, 852 F.2d 612, 615 (D.C. Cir. 1988) (exceptions to the principle that a party must seek timely review of an agency's rulemaking orders are narrowly circumscribed and generally limited to situations such as where the agency did not put aggrieved parties on notice of the rule's content).

In any event, as the FERC orders in this case repeatedly noted (*e.g.*, Pet. App. 35a, 85a-87a, 138a, 148a), any legitimate complaints petitioners may have about the rates CPC will pay MCV for energy from the project are still subject to regulatory oversight by FERC, the Michigan Public Service Commission, and the courts. In particular, FERC properly rejected petitioners' suggestion (Pet. 26-27) that FERC should have taken into account their claim that the rates for MCV power have been or will be set so high that consumers will suffer substantial injury. Under PURPA, the Michigan Public Service Commission—not FERC—must set the rate for MCV energy based on CPC's full avoided cost, *i.e.*, the "cost to the electric utility of the electric energy which, but for the purchase from such cogenerator * * *, such utility would generate or purchase from another source." 16 U.S.C. 824a-3(d). As this Court has observed, "when utilities purchase [such cogenerated electricity] * * *, the rates the utilities charge their customers will not

be increased, for by hypothesis the utilities would have incurred the same costs had they generated the energy themselves or purchased it from other sources." *American Paper Institute*, 461 U.S. at 415 n.9. Insofar as petitioners' true claim is that the Michigan Public Service Commission erred in setting the full avoided cost for MCV power, petitioners' remedy is with that body.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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